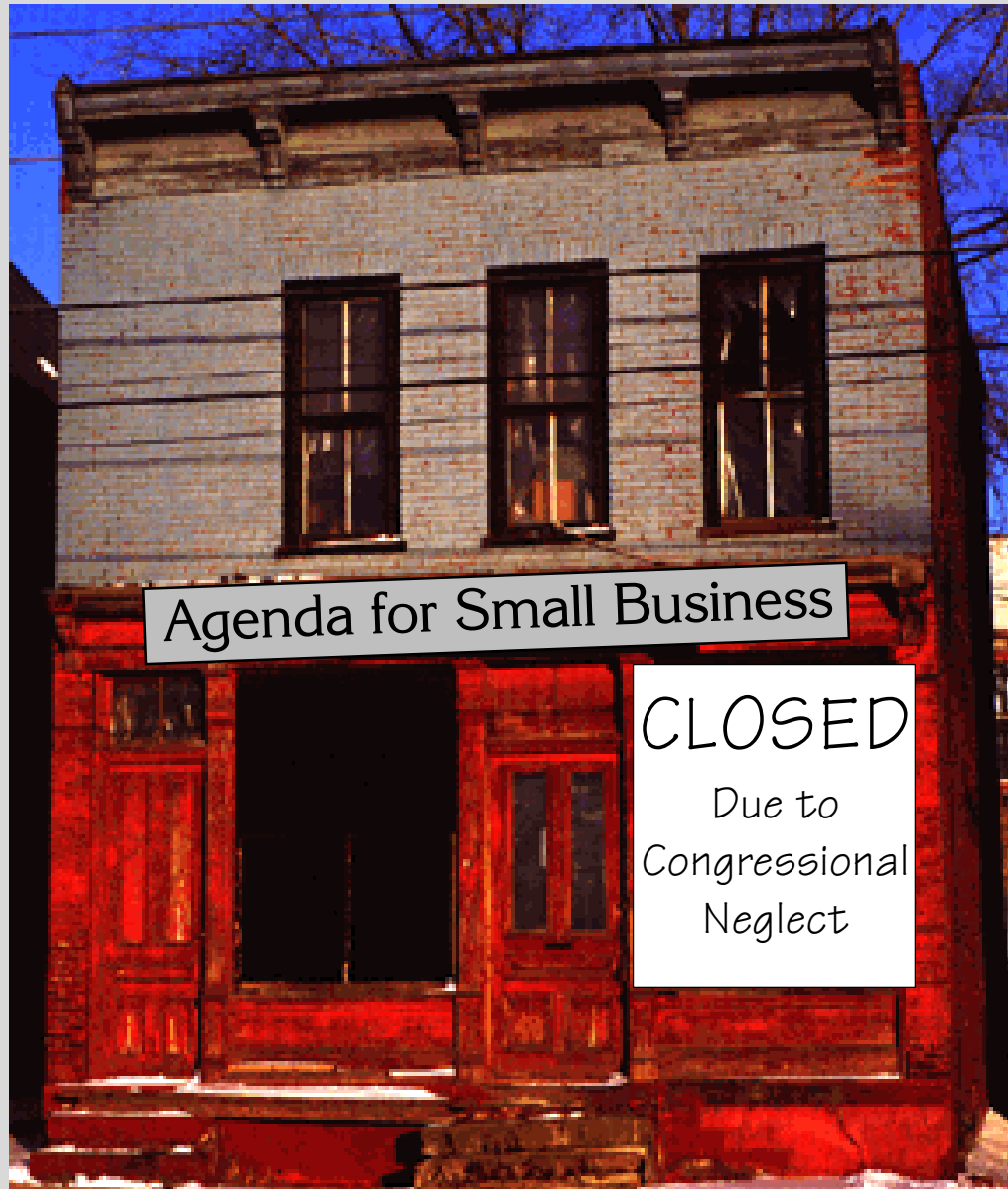


2002 Special Report

America's Small Business Agenda: **CLOSED FOR BUSINESS**



A Report by the Democratic Staff of the
House Small Business Committee
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INTRODUCTION

Small businesses form the backbone of the American economy. They account for half of the gross domestic product and more than half of all existing jobs, and create three-fourths of new jobs each year. They contribute innovations in manufacturing, technology and services. Many of the biggest household name brands today started out small, with just a few employees.

From the corner grocery or dry cleaner to the garage high-tech start-up, small businesses help millions achieve the American Dream through opportunity, hard work and control over one's own destiny. They are the leading vehicle for those traditionally excluded from corporate America. Women-owned businesses nearly doubled during the past decade, and today account for almost 40 percent of private firms. The number of minority-owned enterprises nearly quadrupled in the last decade, and they generally outstrip the national average in business creation and receipts. Americans are starting their own businesses at an increasing and unprecedented rate. The economic opportunity of such enterprise is obvious.

In addition to helping individuals and families, small businesses aid the national economy in ways large companies cannot. Small firms are the first to lead the country out of recession by finding and exploiting niche markets while large corporations shed jobs and avoid risk. During the long boom of the 1990s, small businesses forged the path with new technology, services and innovation to achieve national growth rates economists once thought were just yellowing headlines of a bygone gilded age.

The year 2001 began with great promise for small business. Both Congress and the new Administration repeatedly voiced support of small business and recognized its importance to the nation's economy. The Administration and the 107th Congress promised to be the best for American small business ever.

Unfortunately, that commitment to the entrepreneurial spirit rapidly faded as the country edged into recession. The new Administration and Congressional leadership instead proved to be the best friend big business ever had. The needs of small business, with its great potential to spur economic recovery, were left unaddressed.

Congress failed to provide small businesses with a stimulus package and the recovery tools they need to survive a recession made worse by the events of September 11. Instead, huge tax cuts were granted to big corporations and the wealthy. And the Congressional leadership refused to respond to the concerns of small business on such issues as federal contracting equity, e-commerce, paperwork reduction, advocacy, transportation, worker training, health care, taxes, export and energy policy.

The inertia that held Capitol Hill back on small business issues embodied not only a failure to act on critical issues that have plagued small business for some time, but also in a failure to react to the needs of small business after September 11 left many of them across the nation suffering massive layoffs, lost revenue and even bankruptcy.

Congress did not lack legislative opportunities to help small business. It lacked only the will to help America's entrepreneurs, as well as the understanding that helping small companies across the country is the surest means to help the whole economy out of recession, reduce unemployment, and spark the next long boom.

This report intends to refocus attention and renew interest in the powerful potential of small business to strengthen the economy. During the second session, the Administration is encouraged to join the Congressional leadership in taking up the small business agenda and delivering reforms, reducing taxes and regulations, distributing aid, and improving access to health care. All Americans will benefit from this agenda. Now, it is simply a matter of pushing forward.

METHODOLOGY OF THIS REPORT

This report examines the legislative status of 11 issues critical to small business during the first session of the 107th Congress. The issues were selected based on a survey of 170 small business organizations and trade groups that identified them as priorities for this Congress. They were chosen as a representative cross-section of pressing needs and concerns of American enterprise.

The legislative record was then analyzed to determine how well Congress responded to the small business agenda.

E-COMMERCE

It is estimated that U.S. online transactions will reach nearly \$7 trillion by the year 2006. Given the explosive growth of Internet transactions, more and more small businesses look to increase revenue through the use of e-commerce. In fact, the research firm Dun & Bradstreet reports that 27 percent of small firms with Internet access used this medium for sales transactions in 2001.

One of the primary challenges for small businesses operating within the electronic marketplace is high-speed Internet access, also known as broadband. Although nearly 85 percent of small businesses are already online, only 16 percent of them have high-speed access. This has resulted in small businesses generating, on average, only three online sales per month. High-speed Internet access is the single most important factor contributing to the ability of small firms to increase their online sales.

When small businesses lack high-speed Internet access at reasonable rates, they lag behind in the electronic marketplace. This is of particular concern in sparsely populated regions of the country where companies do not have even the simplest technology due to higher costs and lack of infrastructure. Now, small business owners are beginning to see such access as a national competitiveness issue. Other countries such as Germany and Japan lead the United States in promoting high-speed Internet access for small businesses so they can fully participate in e-commerce across an increasingly wired world.

The Internet and e-commerce have changed the way business gets done. Through the World Wide Web, companies are able to reach a much larger audience, expanding their customer base and boosting revenue. Unfortunately, the Administration and the House leadership have not addressed the real concern of small business access to broadband services. Although several proposals were introduced that outlined the use of tax and other incentives to spur development of broadband capacities, the lack of Congressional action has prevented small businesses from participating to the greatest extent possible in the fast-growing online market. If small businesses wait much longer for action on this issue, they will be left behind in the global, e-commerce driven economy.

ECONOMIC STIMULUS

Small businesses were hit twice and hit hard during 2001. First came a creeping recession early in the year. Then the economy was devastated by the ripple effects of September 11's terrorist attacks. These events combined to hurt small business across the country.

One-third of small firms nationwide reported lower sales after September 11, forcing many of them to shed jobs and put off investment plans. As a result the already soft economy sagged further. Three months later, optimism is up but earnings are still poor and unemployment is on the rise. The recession and terror attacks have put American enterprise in its worst situation in ten years.

Many sectors of small business were especially hurt. The small aviation industry lost \$300-400 million, and motorcoach charters announced cancellation rates of up to 80 percent. Airport concessionaires saw business drop 40-60 percent. Restaurants shed 60,000 jobs nationwide in September alone, and reported that September and October were their worst months on record. Travel agencies lost a staggering \$364 million in sales and \$73 million in commissions the first week after September 11. These companies are looking for aid and relief – assistance Congress has been unwilling to provide them.

While the Administration and House Leadership acted quickly to bail out multi-million-dollar corporations in the airlines and insurance industry, the real needs of small business have been ignored. This has left millions of small company owners on the brink of bankruptcy and closure.

Remedies do exist. Bipartisan legislation, H.R. 3230 (*The American Small Business Emergency Relief and Recovery Act*) would be a powerful and immediate tool to support struggling American entrepreneurs with low- and no-cost loans, grants, and debt forgiveness to help companies make ends meet until the disaster recedes. Unfortunately, the House has not taken up this bill, and small businesses continue to slide into irrecoverable decline.

HEALTH CARE

Small businesses continue the struggle to find adequate, affordable health care coverage for their employees. Today 60 percent of the 43 million Americans without health insurance live in a household with someone employed by a small business. A recent survey of small firms indicated cost was the number one reason why small businesses could not provide health insurance for their workers. In addition to leaving many families without health coverage, cost also puts small businesses at a competitive disadvantage with corporate America in finding and retaining quality employees.

Health costs are again on the rise. From early 2000 to 2001, monthly premiums for employer-sponsored health insurance rose 11 percent. Businesses with fewer than 200 employees faced even higher premium increases, rising 12.5 percent compared to 10.2 percent for larger businesses. This increase in premiums represents the largest since 1992.

In 2001 several bipartisan proposals were introduced to make health care more affordable and accessible. H.R.1774 (*The Small Business Health Fairness Act*) would allow small firms to increase their purchasing power in order to acquire reduced-rate health insurance policies through Association Health Plans (AHPs), just like corporate America. This proposal is estimated to save small businesses and their employees as much as 30 percent on health care costs.

To assist very small businesses and new entrepreneurs, H.R.317 (*The Self-Employed Health Insurance Fairness Act*) would allow the self-employed to immediately deduct the full cost of their health insurance. These entrepreneurs represent over 70 percent of all businesses, but almost 30 percent of them (4.7 million) remain uninsured due to cost.

Both these legislative solutions – AHPs and 100 percent deductibility – are what small businesses need to solve their health care problems. But these proposals to provide affordable health care for millions of Americans remain stalled. Instead, the House leadership continues to push more corporate tax breaks and to restrict the right of patients to hold large HMOs accountable for the care they provide. In the meantime, millions of families employed by small business are forced to live without health care coverage.

ENERGY

Increasing energy costs are an obstacle to growth for many of this nation's small businesses, which operate on very narrow profit margins. The energy crisis that consumed California revealed a frightening new reality: rapid business expansion and increased energy use now can outpace actual energy production. Higher costs and decreased capacity will be more common in the future unless a comprehensive change in energy policy is developed.

Sudden spikes in energy prices have a negative effect on all companies. But the key difference between the long-term impact of these changes on large and small businesses is that large firms have the financial assets to adjust or wait until prices stabilize. That is a luxury that small businesses simply do not have.

Although all sectors of small business get hit by higher costs and lower capacity, the manufacturing industry appears to be suffering the most – it has experienced layoffs and plant closures due to electric and heating bills that doubled or even tripled within a span of a few months. In some areas of the country, energy prices have risen so dramatically that many small businesses face bankruptcy as a result.

Small businesses have called for a national energy policy with specific tax provisions to help them weather hard shifts in energy prices, including the passage of tax incentives and tax credits targeted specifically to small businesses. Proposals would provide an investment tax credit for business investment in renewable energy generation while allowing businesses to take a tax deduction for increasing energy efficiency in non-residential buildings.

But rather than pursue a comprehensive plan aimed at small business energy relief and long-term conservation and efficiency incentives, the proposal adopted last year by the House overwhelmingly favored the corporate energy giants. The legislation pushed to passage in late 2001 supports energy consumption over conservation and provides tax credits, subsidies and incentives worth billions of dollars to wealthy energy-based corporations in the oil, coal, nuclear and automobile industries. In the end, energy powerhouses will reap benefits while small businesses will face a terrible choice between paying steep energy bills or staying in business. Given the important role small businesses play in fueling the nation's economy, there can be no real comprehensive national energy plan without including their interests and views. Unfortunately, not even these preliminary steps were taken last year, and small businesses are left without remedy to spikes in energy costs.

PAPERWORK REDUCTION

Small businesses spend twice as much money per employee complying with federal paperwork requirements as their large corporate counterparts. The smallest firms – those with fewer than 50 employees – spend close to five percent of revenue on paperwork compliance costs. These burdens include OSHA safety records and EPA environmental monitoring records, and, of course, tax documentation that constitutes the majority of paperwork requirements for most enterprises.

Keeping track of and filing paperwork required by various federal agencies takes substantial time away from running a business and often requires significant technical expertise. Compliance costs, compounded by time wasted on paperwork and penalties imposed on businesses that file late or incorrectly, amount to a significant drain of vital resources for small businesses.

The Paperwork Reduction Act of 1980 (PRA) seeks to minimize the cost and burden imposed by federal paperwork requirements on small business and to maximize the utility of the information collected. The PRA creates a system of checks to ensure that agencies do not create new paperwork requirements without prior approval. The PRA authorization lapsed in September 2001, yet there is still a significant amount of unnecessary paperwork that must be eliminated or reduced. It is time to put small business owners back to work, instead of back to filling out forms.

Legislation is pending in Congress (H.R. 327, *The Small Business Paperwork Relief Act*) to require the listing of paperwork requirements by firm size and industry classification. This will make it clear to business owner-operators what paperwork requirements apply to their particular business. However, even this legislation does not address the real problem of reducing the level of paperwork overall. Paperwork reduction efforts must be strengthened to require that agencies actually reduce burdens on small businesses, but Congress has failed to pass a final bill. As a result, small firms continue to bear a disproportionate burden of federal paperwork just to abide by the law.

WORKER TRAINING

Even in a recession, skilled labor is hard to find and comes with a high premium. For example, over the next five years, 500,000 new skilled workers will be needed to meet labor requirements in the construction industry alone. This shortage is expected to last into the foreseeable future as skilled trades continue to be the fastest growing sector of the economy. Failing to address the needs of small business to provide training for a skilled workforce will lower productivity and increase unemployment, exacerbating the recession instead of helping to recover from it.

Recruiting and training workers from a shrinking labor pool, coupled with an economic recession, has become a top concern of small businesses across the country. A recent report stated that workforce education was the top concern for executives at 59 of the 100 largest State and Metro Chambers of Commerce. The skilled labor shortage presents a challenge for small businesses because they must locate and recruit workers and then foot additional costs for apprenticeship training. For small businesses, a four-year training program can cost anywhere from \$84,000 to more than \$200,000 per worker.

High training costs prevent small businesses from offering the kind of opportunities large, deep-pocket corporations can to recruit and retain workers. The Bureau of Labor Statistics reports that workers in businesses with 50-99 employees engaged in formal training only half as long as workers among businesses with at least 500 employees. Less than 19 percent of businesses with fewer than 25 employees maintain formal training programs, compared with 44 percent of firms with 500 or more employees.

Reduced and costly training in highly skilled trades puts small businesses at a competitive disadvantage with larger companies that can more easily afford to train their employees and provide greater career opportunities. Legislation has been introduced to help Main Street businesses compete with Corporate America, but the House Leadership has failed to act on any bill.

H.R. 877 (*The Skilled Workforce Enhancement Act*, or SWEA) has been a small business priority for several years. SWEA would grant small businesses in highly skilled trades a \$15,000 tax credit per employee for the costs of long-term training for up to four years. Given the current economic downturn, a lack of skilled workers and rising unemployment, this bill would help put people to work while filling a small business void in the skilled trades industries. Unfortunately, this common sense proposal continues to languish in the Ways and Means Committee without movement or interest. Small businesses that desperately want to find and retain quality employees have gone another year without new recruitment and training tools from the federal government.

TAXES

Small businesses account for 44 percent of all federal revenue. Taxes hit them doubly hard. First there is the up-front cost of taxes, which is often higher than the corporate rate because self-employed entrepreneurs pay the individual rate. Compounding this are higher compliance costs. Although 90 percent of all companies have assets of less than \$1 million, they spend as much as 27 times more on tax compliance as a percentage of assets than corporations with \$10 billion or more in assets. With small businesses accounting for so much revenue at such high cost, they need tax fairness now more than ever.

Although Congress passed a large tax reduction package in 2001, few of these provisions directly help small companies. This neglectful trend continued with the stalled House economic stimulus measure, which pushed a misguided repeal of the corporate Alternative Minimum Tax (AMT). This proposal would do nothing for Main Street small businesses while giving away billions of dollars to large corporations, including giants such as Texaco and Phillips Petroleum. For instance, Enron would have received over \$250 million from the corporate AMT provision. This proposal shows the House leadership would rather place the fate of the economy with corporate giants instead of the small businesses that actually create the jobs, growth, innovation and technology that can pull the country out of recession.

There are several more practical proposals that would directly assist small businesses, such as H.R. 1037 (*The Small Employer Tax Relief Act*). Small businesses need increased expensing to treat the cost of investments as an ordinary and necessary business expense – this encourages businesses to invest by reducing their up-front tax liability and increasing cash flow. Small businesses could benefit from accelerated depreciation to reduce over-taxing that occurs when businesses invest in equipment. Businesses could then gain from the investment itself, recouping all the capital costs plus more as an effective interest-free “loan” from the government – without costing the government a dime.

TRANSPORTATION AND INFRASTRUCTURE

Small companies across the country rely on our transportation infrastructure to do business. They must be easily accessible to their customers, they must be able to ship and receive goods quickly, and they must have the capacity to travel cheaply, efficiently and reliably to other cities and regions for business purposes. Small businesses cannot rely on a transportation system that is badly in need of repair. The U.S. Department of Transportation reports that 31 percent of our roads are in poor, mediocre, or fair condition, and nearly 29 percent of our bridges are structurally deficient, functionally deficient or obsolete. This disrepair has a real impact on businesses. They must endure endless patch-up repairs and the resulting gridlock that costs them in time wasted and delayed deliveries. It is estimated that an *additional* \$27 billion is needed to improve our nation's surface transportation system.

Though federal transportation spending doubled over the past decade to meet this need, there is more that must be done. Unfortunately, funding for both the Federal Railroad Administration and the Federal Highway Administration was *cut* from its 2001 level, leaving our nation's transportation system to deteriorate even further.

The events of September 11 have brought attention to the security of our transportation infrastructure and the companies that rely on it. Independent general aviation firms, tour bus companies, travel agencies, hotels, restaurants, and concessionaires depend on safe roads, rails and skies for their very survival. These businesses continue to struggle after September 11 and have received no federal grants to help them cope with decreased public travel and a deepening recession. By contrast, the major airlines benefited from a \$15 billion bailout just weeks after the terrorist attacks on New York and Virginia.

Small travel companies have called on Congress to pass legislation to provide security for other modes of transportation (H.R. 3429, *The Motorcoach Security Act*), to promote travel and tourism (H.R. 3321, *The American Travel Promotion Act*), and to provide assistance to small general aviation firms that were grounded for several months. But no action has occurred on any of these high-impact, common sense bills. Instead of aggressively assuring Americans that all modes of travel will remain safe, large corporations have been granted huge bailouts. Small businesses, with thinner profit margins and facing a still-wary public, continue to suffer from this neglect.

FEDERAL PROCUREMENT/CONTRACTING

One of the best ways for small businesses to grow is to have the federal government as a customer. The federal government is the largest buyer of goods and services in the world, with \$200 billion in purchases for fiscal year 2000 alone. Unfortunately, very few of the government's purchases are made from small businesses. In FY 2000, the federal government met none of the goals set by law for contracting with small businesses, including the statutory 23 percent small business goal. The costs of this negligence are extreme: small businesses were excluded from more than \$9 billion in federal contracting opportunities that year.

This has long been recognized as a problem. As far back as 1995, the White House Conference on Small Business made a formal call for equitable treatment of small business in federal procurement. Yet from 1998 to 2000, the number of contracts awarded to small business decreased by more than 14 percent, even while total procurement dollars increased by more than 37 percent during the same period.

Small business groups have well-founded concern that they are losing their share of the federal procurement pie. To address this concern, the bi-partisan bill H.R. 1324 (*The Small Business Contract Equity Act*) was introduced to increase the number of contracts awarded to small businesses by holding federal agencies accountable for their failure to achieve mandated contracting goals. Despite President Bush's campaign call to create more federal contract opportunities for small business, no action has been taken to move this practicable legislation and nothing has been done to increase access to federal contracts. As a result of this neglect, small firms continue to lose business opportunities doing work for the government that could help them grow and create jobs across the country.

EXPORT ASSISTANCE

As the barriers to international commerce continue to crumble due to new technologies, increased transportation options, and reduced tariffs on American exports, small businesses have become a major factor in the global marketplace. In a recent survey, over 200,000 – 97 percent – of all U.S. exporters were small businesses.

No agency is more important to the small business exporter than the Export-Import Bank. The Bank provides loan guarantees, direct loans and political and commercial insurance to enable a small business to export its products and services to emerging markets where, because of political or economic uncertainty, commercial lenders will not provide financial assistance. In FY 2000, the Bank's programs supported over \$5 billion in exports for more than 2,000 small businesses.

Small businesses and the associations that represent them have called for full reauthorization of the Export-Import Bank and an increase in its budget. However, neither of these goals has been achieved. Instead of increases, the FY 2002 Export-Import Bank program budget was *reduced* by 10 percent. Furthermore, the full Congress has yet to act on H.R. 2871, legislation to reauthorize the Bank. Small business growth in the global marketplace should not be limited by budget cuts and restrictions on the assistance programs provided by the Export-Import Bank. Instead, Congress must reauthorize the Export-Import Bank and fully fund the program, so that small businesses can continue to expand their market reach.

SMALL BUSINESS ADMINISTRATION OFFICE OF ADVOCACY

As this report clearly indicates, the needs of small business are routinely overlooked. It is the job of SBA's Office of Advocacy to give small business an independent voice before Congress, federal regulators, the White House and state policy makers. The Office of Advocacy serves as the watchdog for small businesses and the champion of their interests on a national scale.

The Office of Advocacy pursues its mission by monitoring 80 federal agencies that promulgated more than 8,000 rules, taking up 70,000 pages of the Federal Register in 1999 alone. Advocacy also educates policymakers on the important role small businesses play in this country by maintaining economic data and surveying the most pressing issues facing entrepreneurs.

Advocacy is a powerful defender of small business, pursuing its mission with less than 1% of the SBA's budget. But during the last decade, its resources have become more and more scarce, and the size of the office has been cut almost in half. Bipartisan legislation has been introduced to protect the Office of Advocacy from further cuts and to strengthen its independence as an uncompromised voice for small business. This proposal saw no House action during the first session of 107th Congress. The result is a quieter, less effective voice in defense of small business in government.

CONCLUSION: **REFOCUSING ON SMALL BUSINESS**

American small business started the 107th Congress with high hopes and a big agenda. A Congress and new Administration with avowed sympathies for American entrepreneurship took power, promising to be the best ever for small companies. The issues were many and critical.

Small businesses want broadband access so they can exploit the full e-commerce potential of the Internet. They worry about dilapidated transportation infrastructure, slowing the travel of goods to market and employees to work. A lackluster national energy policy has placed small companies at the mercy of spikes in fuel cost. Regulatory paperwork continues to eat up time better spent serving clients and customers. Hiring and retaining qualified workers with costly training programs and health benefits remain a major concern for trades and small companies. Taxes still hit small business much harder, proportionally, than they do their corporate counterparts. And they would still like to see something for them in an economic stimulus package that currently gives the most and the best to the largest corporations.

But Congress rapidly lost focus on small companies at exactly the time when they needed help most. As the economy weakened and it became clear the country had entered a recession, the Administration and Congressional Leadership instead focused their aid on corporate America. Unfortunately, in doing so they ignored the powerful contributions small businesses made to lifting this country out of the recession of the early 1990s and spurring the greatest peacetime economic expansion in history.

American enterprises did it before, and they can do it again. It is especially important now, in a period of high unemployment and economic contraction, that Congress and the Administration refocus on the small business agenda for the second session. If they take up these crucial issues, they will quickly help entrepreneurs in ways that will benefit all of us – with more jobs, higher growth, and new innovations in technology and services.

If our leaders do not help small business at this critical time, the country risks returning to the economic mire of the early 1990s – and staying there.

The agenda is clear. The question now is whether Congress will act.